IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

GIFT TAX REFERENCE No 2 of 1984

For Approval and Signature:

Hon'ble MR.JUSTICE R.BALIA. and
MR.JUSTICE A.R.DAVE

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1. Whether Reporters of Local Papers may be allowed to see the judgements?

2. To be referred to the Reporter or not?

3. Whether Their Lordships wish to see the fair copy of the judgement?

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder?

5. Whether it is to be circulated to the Civil Judge?

COMMISSIONER OF GIFT-TAX

Versus

PRTHIVI NATH SHRAMA

Appearance:

MR MANISH R BHATT for Petitioner

SERVED BY RPAD - (N) for Respondent No. 1

CORAM : MR.JUSTICE R.BALIA. and
MR.JUSTICE A.R.DAVE

Date of decision: 11/11/98

ORAL JUDGEMENT

1. At the instance of Commissioner of Gift Tax, Baroda, following question of law arising out of its order dated 7.1.1983 by the Income Tax Appellate Tribunal, Ahmedabad has been referred to this court for its opinion:

"Whether, on the fact and in the circumstances of the case, the Tribunal was right in law in coming to the conclusion that Rule 1D of the W.T. Rules were applicable for determining the value of the unquoted shares for the purpose of the Gift-tax"

2. The respondent assessee had made a gift of certain shares of private limited companies. The shares were not quoted on the Stock Exchange. As shares were of private limited company, free transfer of which was prohibited under its memorandum of association and were not quoted at Stock Exchange to determine its price on the date of gift, the value of shares gifted was worked out at Rs.31,000/-. The assessee claimed a deduction of 15% of such sum by inviting attention to Rule 1D of the Wealth Tax Rules. The Income Tax Officer rejected the claim of the assessee for adjusting the value of shares gifted for the purpose of levying gift tax. On appeal, the learned Appellate Assistant Commissioner, agreed with the claim of the assessee, and directed the Gift Tax Officer to recompute the value of gift for the tax purposes. On further appeal, the Tribunal agreed with the view taken by learned Appellate Assistant Commissioner following its own earlier decision and a decision of the Bombay Tribunal. In these circumstances, the aforesaid question has been referred to us.

3. Heard learned counsel for the parties. At the relevant time, to which the assessment in question relate, Section 6 which provided for valuing the gifts read as under:

"6. Value of gifts, how determined.-(1) The value of any property other than cash transferred by way of gift, shall, subject to the provisions of sub-sections(2) and (3), be estimated to be the price which in the opinion of the Assessing Officer, it would fetch if sold in the open market on the date on which the gift was made.

(2) Where a person makes a gift which is not revocable for a specified period, the value of the property gifted shall be the capitalised value of the income from the property gifted during the period for which the gift is not revocable.

(3) Where the value of any property cannot be estimated under sub-section (1) because it is not saleable in the open market, the value shall be determined in the prescribed manner."

Subsection (2) deals with the value of the revocable gifts with which we are not concerned. Subsection (1) furnishes basic principle of valuing gifts other than cash to be valued at the open market price of the asset, if sold on the date on which the gift was made. Subsection (3) deals determination of value of such asset which is not saleable in the open market to be determined in the prescribed manner. Rule 10(2) which is relevant for our purposes deal with valuation of shares of private companies whose articles of association contains restrictive provisions as to the alienation of shares, if not ascertainable by reference to the value of total asset of company is to be estimated to be what the same would fetch if on the date of gift could be sold in the open market on the terms of purchaser being entitled to be registered as holder subject to articles. In terms it makes it clear that the fact that a special buyer for his own special reason give a higher price than the price in the open market shall be disregarded. Thus it will be seen that estimate of value of the gift with reference to its market price is not altogether excluded even in the case if the same are not saleable in the open market and the open market price is not available. The question really is therefore how the price of such shares which are not saleable in open market where there is a restriction in sale of shares, is to be determined. The value is to be determined as on the date of the gift. The break up value of the shares of a company in commercial parlance is determined by deducting the value of all the liabilities as shown in the balance sheet of the company from the value of all its assets shown in that balance sheet. The net amount so arrived at is then divided by the total amount of its paid up equity share capital as shown in the balance sheet. The resultant amount multiplied by the paid up value of each equity share is to be treated as break up value of each unquoted share of the company. However, as observed by Williams, J in McCathie v. Federal Commissioners of Taxation (69 CLR 1) which has been approved by their Lordships of Supreme Court in Commissioner of Gift-tax, Gujarat v. Executors and Trustees of the Estate of Late Sh. Ambalal Sarabhai (1988) 170 ITR 144, that break up value represents the amount which the share holders are likely to realise upon the liquidation and does not reflect the real value as on the date when it is being considered. Obviously the estimated value as on that date of break up value, needs adjustment to make the estimate of value as on that date to be realistic, if the said method is to be adopted. One illustration is provided under the Rules framed for valuing any asset as on the valuation date for the purpose of the Wealth Tax Act. Like Section 6 of the

Gift Tax Act, Section 7 of the Wealth Tax Act too provide for the determination of the value of assets held by an assessee as on the valuation date. At the relevant time subsection (1) of Section 7 which is para materia with subsection (1) of Section 6 read:

"7. Value of assets, how to be determined. - (1) Subject to any rules made in this behalf, the value of any asset, other than cash, for the purposes of this Act, shall be estimated to be the price which in the opinion of the Assessing Officer, it would fetch if sold in the open market on the valuation date."

Rule 1D which prescribe for determining market value of unquoted equity shares of any company other than investment or a managing agency company so far as relevant for the present purposes reads as under:

"The value of all the liabilities as shown in the balance sheet of such company shall be deducted from the value of all its assets shown in that balance sheet. The net amount so arrived at shall be divided by the total amount of its paid-up equity share capital as shown in the balance sheet. The resultant amount multiplied by the paid-up value of each equity share shall be the break up value of each unquoted equity share. The market value of each such share shall be 80 per cent of the break up value so determined"

A perusal of this provision goes to show that a distinction is made between the term break up value and `market value'. This clarifies the distinction between the principle that the break up value represents the value of the share on realisation of the companies assets on liquidation whereas the present market value as on the date with reference to which the value of asset has to be determined requires adjustment. A statutory guideline was fixed in order to remove disparity in such discounting by different assessing authorities by providing a standard yardstick under the rules. Under Rule 10 of the Gift Tax Rules it would be noticed that term used is not that the value of share shall be `the break up value' of shares as on the date of the Gift but it only provides `finding value with reference to total assets of the company'. This clearly goes to show that under the Rule too, break up value as such has not been prescribed to be the value of the gift as on the date for the purpose of levying tax, but, the break up value has

only been provide as a foundation on the basis of which the value is to be determined by the assessing officer and where assessing officer is not able to ascertain, then, he has to fall back on the open market price formula, by assuming that the shares are transferable. If that be so, then, in considering the question of adjustment of break up value, a fair amount of deduction is to be considered to ascertain its present value on the date of gift, due to factors like the inalienability of the shares, the difficulty in finding a buyer, or obtaining consent of the company for alienation of shares to each person, and the like circumstance which cannot be exhaustively enumerated. The discounting of such break up value has been accepted to be admissible formula for arriving at the value of such asset as on the date with reference to which it is to be determined. This being the question we find that it cannot be said that Tribunal was not justified in applying the principle of reducing the amount of the break up value. Once it is granted on principle that some amount can be adjusted against the break up value, what should be the deductible amount will be a matter of exercise of fair amount of discretion on the part of the assessing authority. If in doing so, he falls back on a statutory guideline provided in the cognate statute for the like purpose, in the absence of any such guideline under the statute for which such exercise is undertaken it cannot be said that adoption of such formula to be perverse. We hasten to add that the provisions of any other statute would not apply ipso facto as a matter of course, while considering assessments under one Act. The assessee or for that matter the assessing authority cannot claim as a matter of law the applicability of any provision or rule framed under the wealth Tax or for that matter in other statute to be applicable to proceedings under Gift Tax Act a fortiori on their own force. However, in culling out the principle and guideline to be applied in framing assessment under Gift Tax Act if there is no specific provision under the Act, the assessing authority can always look around the guidelines emerging for like situations under other statutes without surrendering to such statutes as a matter of course. We find from the order of the Tribunal that by relying on a decision of the Bombay Tribunal which has accepted the principle of deduction to be considered for the purpose of valuing the shares under Rule 10(2). The reference to Rule 1D of Wealth Tax Rules was referred only as statutory guidance available in the matter. No fault can be found with this reasoning that though Wealth Tax Rules are not applicable and cannot be imported on their own for proceeding under the Gift Tax Act in the absence of any specific provision

under the Gift Tax Act, in the matter of exercise of discretion, for determination of valuation of assets as on a particular date guiding light can be seen.

In this connection reference may also be made to a Bench decision of Madras High Court in Commissioner of Gift-tax, TamniNadu-III v. S. Venu Srinivasan and Another (1978) 112 ITR 771. The facts were similar to the present case. The shares of a private limited company were gifted. The shares were not saleable in the open market on the date of gift. Therefore, the case fell under Section 6(3) of the Gift Tax Act and applicability of Rule 10(2) was invited. The Tribunal accepted the valuation of shares as on the date of gift not at the break up value, but, at a lesser rate than the break up value, as its market price on that date. On a reference at the instance of Revenue. The Court opined:

"That even in such cases under rule 10(2) of the Gift Tax Rules, 1958, it should be assumed that the shares were capable of being sold freely in the open market and that there would be purchasers for the same. Therefore, it will be necessary to ascertain what the shares of a private limited company would fetch if sold in a hypothetical market which may not really exist. However, the value the shares of a private limited company would fetch in the open market as ascertained disregarding the restrictions as to sale will have to be reduced because in reality the shares would not fetch that much of money when transferred because the shares in a private limited company are not easily transferable and hence cannot be treated to be on a par more or less with money that can be handed over quickly from one person to another or other commodities which are readily saleable."

Apart from the above principle, we find from the statement of case as well as from the annexures appended thereto, it is nowhere to be found that value of shares at Rs.31000/- has been worked out at break up value. In the absence of this basic finding, that value of shares was worked out at Rs.31000/- as per the break up value by deducting total liability of the company from its total value of assets, it would be groping in dark to search for exact principle to be applicable in the present case, namely, whether, the value was fixed as per the break up method or by adopting estimated value of the shares as if, they were to be sold in open market and the price it would fetch on such sale.

4. In the aforesaid circumstances, we answer the question referred to us by holding that Rule 1D of Wealth Tax Rules does not apply to the gift tax proceedings by its own force but in determining the value of gift as on the date, of gift in terms of section 6 in the absence of any guideline under the Rules under the Gift Tax, in the facts and circumstances of this case the Tribunal was justified in adopting the principle for making adjustment to arrive at market value of the shares in question as on the date of gift.

There shall be no orders as to costs.

(Rajesh Balia, J)

(A.R. Dave, J)